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February 19, 2016

VIA ECFS

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: ***Special Access for Price Cap Local Exchange Carriers, WC Dkt. No. 05-25;
AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local
Exchange Carrier Rates for Interstate Special Access Services, RM-10593***
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Dear Ms. Dortch:

On behalf of Birch Communications, Inc., EarthLink, Inc., and Level 3 Communications, LLC (collectively, the “Joint CLECs”), I hereby submit the redacted version of the Joint CLECs’ reply comments in response to Section IV.B of the Further Notice of Proposed Rulemaking released on December 18, 2012 in the above-referenced proceeding.¹ These redacted materials are being submitted pursuant to the terms of the *Modified Protective Order*,² *Second Protective*

¹ *Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, Report and Order and Further Notice of Proposed Rulemaking, 27 FCC Rcd. 16318 (2012).

² *Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, Modified Protective Order, 25 FCC Rcd. 15168 (2010).

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Order,³ and *Data Collection Protective Order*⁴ in effect in this proceeding. Pursuant to the procedures outlined in the *Data Collection Protective Order*, the original Highly Confidential version of this submission has been submitted to the Secretary's Office and two copies of the Highly Confidential version of this submission have been delivered to Mr. Christopher Koves in the Pricing Policy Division of the Wireline Competition Bureau under separate cover.

Please contact me at (202) 303-1111 if you have any questions regarding this submission.

Respectfully submitted,

/s/ Thomas Jones

Thomas Jones

*Counsel for Birch Communications, Inc.,
EarthLink, Inc., and Level 3
Communications, LLC*

Attachments

³ *Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, Second Protective Order, 25 FCC Rcd. 17725 (2010).

⁴ *Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, Order and Data Collection Protective Order, 29 FCC Rcd. 11657 (2014) ("*Data Collection Protective Order*"); see also *Wireline Competition Bureau Now Receiving Acknowledgments of Confidentiality Pursuant to Special Access Data Collection Protective Order*, Public Notice, 30 FCC Rcd. 6421 (2015).

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**Before the
Federal Communications Commission
Washington, D.C. 20554**

In the Matter of)	
)	
Special Access Rates for Price Cap Local)	WC Docket No. 05-25
Exchange Carriers)	
)	
AT&T Corporation Petition for Rulemaking to)	RM-10593
Reform Regulation of Incumbent Local Exchange)	
Carrier Rates for Interstate Special Access)	
Services)	

**REPLY COMMENTS OF
BIRCH, EARTHLINK, AND LEVEL 3**

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**REPLY COMMENTS OF
BIRCH, EARTHLINK, AND LEVEL 3**

Birch Communications, Inc., EarthLink, Inc., and Level 3 Communications, LLC (“Level 3”) (collectively, the “Joint CLECs”), through their undersigned counsel, hereby submit these reply comments in response to Section IV.B of the Further Notice of Proposed Rulemaking released on December 18, 2012 in the above-referenced proceeding.¹

I. INTRODUCTION AND SUMMARY

The Joint CLECs, similarly-situated commenters, and expert economists have conclusively demonstrated that incumbent LECs possess substantial and persisting market power

¹ *Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, Report and Order and Further Notice of Proposed Rulemaking, 27 FCC Rcd. 16318 (2012). Although Section IV.B of the Notice of Proposed Rulemaking seeks comment primarily on reform of pricing flexibility triggers, it also seeks comment more generally “on what steps the Commission should take where relief has been provided under our existing rules and where the data and our analysis demonstrate that competition is not sufficient to discipline the marketplace.” *Id.* ¶ 80. These reply comments focus primarily on these broader issues in support of the framework for the comprehensive review and reform of the markets for dedicated services in the U.S. proposed in the comments filed by the Joint CLECs on January 27, 2016.

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in the provision of dedicated services.² The source of this market power is the incumbent LECs' ownership of the only connection to the vast majority of commercial buildings where customers demand dedicated services (*i.e.*, "locations"). Moreover, the existing regulatory regime governing incumbent LEC dedicated services does not come close to preventing the incumbent LECs from abusing their market power. As a result, the incumbent LECs charge prices above efficient levels, and they condition the availability of "discounts" off of those prices on exclusionary volume and term commitments that lock up the wholesale market and suppress competition ("lock-up plans"). The Commission should therefore adopt a comprehensive regulatory regime designed to stop this harmful conduct, one that includes *ex ante* rate regulations and prohibitions against unreasonable volume and term lock-up plans.

Notwithstanding the facts, the incumbent LECs argue that the Commission need not worry about their monopoly over connections because competitors can supposedly deploy connections virtually anytime and anywhere they want. They therefore argue that the mere presence of fiber in a census block or zip code is evidence of competition. This argument has never made any sense because it ignores the substantial barriers competitive carriers must overcome to construct connections. But there is now empirical evidence that it is flatly wrong. It has been 20 years since the passage of the 1996 amendments to the Communications Act removed the legal barriers to local competition and opened the market to entry. During that time,

² As used in these reply comments, the terms "dedicated service," "connection," and "location," have the meaning defined in the special access mandatory data request. *See Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, Order on Reconsideration, 29 FCC Rcd. 10899, App. A (2014). In addition, the terms "loop" and "connection" are used interchangeably in this filing.

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competitors have succeeded in deploying connections to **[BEGIN HIGHLY CONFIDENTIAL]** **[END HIGHLY CONFIDENTIAL]** percent of the locations in the country. This is an **[BEGIN HIGHLY CONFIDENTIAL]** **[END HIGHLY CONFIDENTIAL]** percentage.

Moreover, there is simply no basis for predicting that competitive carriers will deploy connections to a large number of locations in the future. As demonstrated in the declaration of John Merriman of Level 3 attached hereto as an Appendix, even a competitive LEC like Level 3, which owns an extensive fiber transport network, can deploy loops to, at most, approximately **[BEGIN HIGHLY CONFIDENTIAL]** **[END HIGHLY CONFIDENTIAL]** percent of the commercial buildings in the ten most populous metropolitan statistical areas (“MSAs”) in the country. Nor is there reason to think that other competitive carriers, including cable companies, could deploy connections at a significantly faster pace, because all competitive carriers face the same barriers to deploying connections.

Finally, while the incumbent LECs try to salvage their argument by pointing to the availability of best efforts broadband services and fixed wireless services, these services have no effect on the incumbent LECs’ market power in the provision of dedicated services. This is because, as the record in this proceeding abundantly demonstrates, neither of these services is a substitute for wireline dedicated services.

II. THE INCUMBENT LECS HAVE SUBSTANTIAL AND PERSISTING MARKET POWER IN THE PROVISION OF DEDICATED SERVICES

A. The Incumbent LECs’ Monopoly Over Connections Gives Them Market Power in the Provision of Dedicated Services

The record in this proceeding shows that the incumbent LECs own the only connection to approximately **[BEGIN HIGHLY CONFIDENTIAL]** **[END HIGHLY CONFIDENTIAL]**

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percent of the commercial buildings served by dedicated services in the U.S.³ This is the decisive fact in this proceeding. Given the high barriers that all competitive carriers, both traditional competitive LECs and cable companies, must overcome to deploy new connections, the incumbents' control over connections gives them largely unfettered freedom to set prices for dedicated services above competitive levels and to use lock-up plans to prevent wholesale competition from developing. The Joint CLECs and similarly-situated commenters have demonstrated at length that the incumbent LECs are doing just that.

Faced with these facts, now comprehensively documented, the incumbent LECs try to argue that the mere presence of fiber transport facilities deployed by *one* non-incumbent LEC in a census block or zip code disciplines the rates, terms, and conditions on which the incumbent LECs offer dedicated services.⁴ This is a fantasy. The presence of nearby fiber-transport facilities is obviously not evidence of *actual* competition, because a competitor must incur significant sunk costs in order to deploy a connection from its transport facilities to a location in order to reach the customer.⁵ It follows that the presence of a competitive LEC's fiber near a building is, at most, *potential* competition. But potential competition can only limit an incumbent LEC's ability to increase price above competitive levels if a competitive carrier's

³ See Declaration of Dr. Jonathan B. Baker on Market Power in the Provision of Dedicated (Special Access) Services, ¶ 44 (Jan. 22, 2016) (*attached to* Letter from Dr. Jonathan Baker, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, RM-10593 (filed Jan. 27, 2016)) ("Baker Decl.").

⁴ See, e.g., AT&T, Inc. Comments, WC Docket No. 05-25, RM-10593, at 7, 11-17 (filed Jan. 28, 2016) ("AT&T Comments"); Verizon Comments, WC Docket No. 05-25, RM-10593, at 24-28 (filed Jan. 28, 2016) ("Verizon Comments"); CenturyLink Comments, WC Docket No. 05-25, RM-10593 at 6-11 (filed Jan. 28, 2016) ("CenturyLink Comments").

⁵ See Baker Decl. ¶ 40.

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deployment of connections is timely, likely, and of sufficient scale to counteract a price increase by the incumbent LEC.⁶ Determining whether this is the case requires consideration of “barriers to entry such as high capital expenditures, large sunk costs, long lead times, scale economies, and cost disadvantages.”⁷ These factors all support the conclusion that the presence of nearby fiber-transport facilities could only discipline the incumbent LEC in unusual circumstances.

Barriers to loop deployment. The ILEC Economic Analysis acknowledges, as it must, that competitive carriers incur sunk costs when deploying connections, but it states (without any factual support) that “extending laterals requires a significantly smaller capital expenditure per unit of bandwidth, *making this a relatively low-cost expansion.*”⁸ The incumbent LECs essentially build their entire argument on this assertion. It is, of course, incorrect.

As the Joint CLECs explained in their comments, competitive LECs “face ‘substantial operational barriers’ to deploying their own facilities.”⁹ In his declaration, Mr. Merriman describes the obstacles that affect Level 3’s deployment costs as including “access to pole attachments, differences in terrain, permitting costs, repaving requirements, and moratoriums due

⁶ Comments of Birch, BT Americas, EarthLink, and Level 3, WC Docket No. 05-25, RM-10593, at 32 (filed Jan. 27, 2016) (“Joint CLECs Comments”).

⁷ *Id.* (citing U.S. Department of Justice & Federal Trade Commission, *Commentary on the Horizontal Merger Guidelines*, at 38 (Mar. 2006), <http://usdoj.gov/atr/public/guidelines/215247.pdf>; ABA Section of Antitrust Law, *Antitrust Law Developments*, at 351 (6th ed. 2007)); *see also* Baker Decl. ¶¶ 96-98.

⁸ Mark Israel et al., *Competitive Analysis of the FCC’s Special Access Data collection*, White Paper, at 10 (Jan. 26, 2016) (*attached to* Letter from Glenn Woroch, Compass Lexecon, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, at 10 (filed Jan. 28, 2016)) (“ILEC Economic Analysis”) (emphasis added).

⁹ Joint CLECs Comments at 33 (quoting *Unbundled Access to Network Elements; Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, Order on Remand, 20 FCC Rcd. 2533, ¶ 151 (2005) (“*Triennial Review Remand Order*”)).

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to weather.”¹⁰ Other competitive LECs have reported similar impediments affecting their cost of deploying additional connections.¹¹ Importantly, these sunk costs are in addition to the costs associated with deploying fiber transport facilities. They therefore constitute a barrier to connection deployment that is *independent of the deployment of fiber transport networks*.

Moreover, these sunk costs are high enough and the deployment of loops is uncertain enough that connection deployment is frequently uneconomic where a competitive LEC has deployed fiber transport facilities near to the customer location. As Mr. Merriman explains, notwithstanding its extensive fiber transport network, “it is rarely possible for Level 3 to deploy its own fiber optic loop facilities to commercial buildings.”¹² XO, which also has extensive fiber transport facilities, frequently cancels otherwise economic construction plans due to the various costs and risks associated with connection deployment.¹³ XO explains that “[s]uch additional and unexpected costs or hurdles arising from public ROW access and dealing with building owners and landlords often lead XO to cancel a build that otherwise may be economic.”¹⁴ As

¹⁰ Declaration of John Merriman on Behalf of Level 3 Communications, LLC, ¶ 6, attached hereto as an Appendix (“Merriman Decl.”).

¹¹ Windstream Services, LLC Comments, WC Docket No. 05-25, RM-10593, GN Docket No. 13-5 at 35 (filed Jan. 28, 2016) (“Windstream Comments”); *see also* TDS Metrocom, LLC Comments, WC Docket No. 05-25, RM-10593, at 18-19 (filed Jan. 28, 2016) (“TDS Comments”) (explaining that “deployment cost is highly distance-sensitive” and that by comparison, an incumbent LECs, such as AT&T, has significant cost advantages as its territory tends to be “much more urban with greater business density” and its network is already built closer to more customers than competitive LECs’ networks).

¹² Merriman Decl. ¶ 10.

¹³ XO Communications, LLC Comments, WC Docket No. 05-25, RM-10593, at 14 (filed Jan. 27, 2016) (“XO Comments”).

¹⁴ *Id.*

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Windstream explains, “even the largest competitive providers have not been able to build their own last-mile facilities to more than a small fraction of all the business buildings to which the ILECs have connectivity by virtue of their incumbency,” because “widespread CLEC last mile build-outs to business customers remain economically infeasible today.”¹⁵

Past attempts to deploy loops. Competitive carriers’ past attempts to deploy connections powerfully demonstrate that such deployment is possible in only rare circumstances. The numbers speak for themselves. In the 20 years since the 1996 amendments to the Communications Act eliminated the legal barriers to local competition and opened the market for entry, competitive LECs have deployed connections to only approximately **[BEGIN HIGHLY CONFIDENTIAL]** **[END HIGHLY CONFIDENTIAL]** percent of the locations in the U.S. In addition, as the Joint CLECs explained in their comments, most of the competitive carriers that deployed local transmission facilities, including connections, in the past ended up in bankruptcy. This indicates that the deployment of local transmission facilities was uneconomic in many circumstances – so uneconomic, in fact, that it destroyed most of the companies that attempted it.¹⁶ This history of repeated failure has made existing competitors justifiably selective and cautious when considering the deployment of new connections.

Level 3’s experience illustrates the excruciatingly slow pace of competitive LEC connection deployment. Level 3 has deployed connections **[BEGIN HIGHLY CONFIDENTIAL]** **[END HIGHLY CONFIDENTIAL]**

¹⁵ Windstream Comments at 36, 39; *see also* XO Comments at 16 (“XO’s networks still largely reach only a relatively small fraction of MTEs and other commercial buildings in core areas of select major metro areas”); TDS Comments at 21-22.

¹⁶ *See* Joint CLECs Comments at 36-37, Appendix D.

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competitive carriers. But so far Level 3 has only deployed connections to approximately 34,000 commercial buildings in the U.S.¹⁷ Given that there are approximately [BEGIN HIGHLY CONFIDENTIAL] [END HIGHLY CONFIDENTIAL] unique locations in the U.S. as of 2013 where customers utilize dedicated services, this means that Level 3 has deployed connections to only approximately [BEGIN HIGHLY CONFIDENTIAL] [END HIGHLY CONFIDENTIAL] percent of the locations in the U.S. Moreover, as Mr. Merriman explains in his declaration, Level 3 has deployed connections to [BEGIN HIGHLY CONFIDENTIAL] [END HIGHLY CONFIDENTIAL] percent of the commercial buildings (as defined by the CoStar Group) in the ten most populous MSAs in the country.¹⁸

Prospects for future deployment of connections. Competitive carriers' prospects for future deployment of connections confirm that the incumbent LECs will continue to own the only connection to the vast majority of locations for many years. Again, Level 3's experience illustrates the problem. Level 3 aims to build new connections to approximately 3,000 to 4,000 locations per year.¹⁹ At this pace, it will take Level 3 roughly [BEGIN HIGHLY CONFIDENTIAL] [END HIGHLY CONFIDENTIAL] years to deploy connections to just half of the locations in the U.S.

To further illustrate this problem, Mr. Merriman conducted an analysis to identify the number of commercial buildings that are potential loop deployment targets for Level 3 in the ten most populous MSAs in the country. As Mr. Merriman explains, Level 3 evaluates all potential

¹⁷ *Id.* at 7.

¹⁸ Merriman Decl. ¶ 10 Tbl. 2.

¹⁹ Joint CLECs Comments at 7.

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build-out opportunities “with respect to the estimated capital expenditure that would be necessary and the expected revenue that would result from the build out.”²⁰ To conduct this evaluation, Level 3 follows certain guidelines, under which it considers **[BEGIN HIGHLY CONFIDENTIAL]**

²¹ **[END HIGHLY CONFIDENTIAL]**

Utilizing these guidelines, as well as certain conservative assumptions, Mr. Merriman estimates that approximately **[BEGIN HIGHLY CONFIDENTIAL]** **[END HIGHLY CONFIDENTIAL]** percent of the commercial buildings in the ten most populous MSAs in the U.S. either meet Level 3’s potential target criteria for loop deployment or are buildings to which Level 3 has already deployed a loop.²² This is **[BEGIN HIGHLY CONFIDENTIAL]**

[END HIGHLY CONFIDENTIAL] percentage. It confirms that the threat of competitive LEC connection deployment in the future cannot possibly discipline incumbent LECs in their provision of dedicated services.

But even the estimates in Mr. Merriman’s declaration overstate the extent to which Level 3 could deploy connections in the future. As Mr. Merriman explains, there are a number of factors that prevent Level 3 from deploying connections to locations that otherwise meet its

²⁰ Merriman Decl. ¶ 7.

²¹ *Id.*

²² *Id.* ¶ 12 Tbl. 3.

targeting criteria.²³ For example, Level 3 is often unable to win a high enough percentage of the revenues in a building to justify deployment of a loop. This can be for any number of reasons, including customers' unwillingness to "break the bundle" of services that it purchases from the incumbent LEC.²⁴ In addition, problems associated with obtaining access to multi-unit buildings sometimes prevent Level 3 from serving customers in such buildings.²⁵ This is a problem that incumbent LECs appear not to experience in the same way given their legacy relationships with the owners of most buildings. Finally, the cost of leasing incumbent LEC connections needed to reach off-net locations of multi-location customers sometimes prevents Level 3 from being able to justify the deployment of loops even to customer locations that would otherwise meet Level 3's build criteria.²⁶

Cable companies. The incumbent LECs never fail to identify a source of potential future entry that will purportedly deliver American businesses from the grip of the incumbents' market power over dedicated services at some point in the undefined future. There is a long, and rather depressing, history of these unfounded predictions. The incumbents' latest theory is that cable companies will make the market for dedicated services competitive. But it is already clear that the cable companies do not and cannot possibly compete on the scale needed to discipline the incumbent LECs in the provision of dedicated services.

²³ *Id.* ¶¶ 14-17.

²⁴ *Id.* ¶¶ 14-15.

²⁵ *Id.* ¶ 16.

²⁶ *Id.* ¶ 17.

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The cable companies have historically focused on providing mass market services. As the Commission recognized several years ago, “most of the businesses served by cable companies are not large enterprise customers, but mass market small businesses that would never generate enough traffic to require a high-capacity loop” and “where cable companies do provide service to business customers, they provide cable modem service, rather than service that is comparable to service provided over high-capacity loops.”²⁷ Importantly, this remains largely true today. As one analyst and former Chief of the Commission’s Office of Strategic Planning and Policy Analysis observed last year, cable companies have been able to serve residential, small-, and medium-sized regional businesses “using only-slightly-adapted consumer products,” but they “ha[ve] been largely unable to serve the more complex segments.”²⁸ This means that cable companies have not deployed connections on a widespread basis.

Moreover, cable companies face the same barriers to deploying new loops for the provision of dedicated services that traditional competitive LECs face. Given that even Level 3, with its extensive fiber transport network, will not be able to deploy new connections to the

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commercial buildings in the ten most populous MSAs, it is unlikely that any cable company

could deploy new loops [BEGIN HIGHLY CONFIDENTIAL]

[END

HIGHLY CONFIDENTIAL] of commercial buildings.

²⁷ See *Triennial Review Remand Order* ¶ 193; Joint CLECs Comments at 14-15 n.25.

²⁸ See Paul de Sa et al., *U.S. Telecom: A Primer on the \$70B Enterprise Telecom Market (Cable’s Opportunity = Telcos’ Loss?)*, Bernstein, at 6 (July 16, 2015).

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The incumbent LECs try to hide the cable companies' limited deployment of connections by relying on cable companies' aggregate revenues from business services and the total number of commercial buildings they serve.²⁹ However, the revenue statistics do not differentiate between revenues generated by the sale of dedicated services and revenues generated by the sale of best efforts services. And, the commercial building statistics do not differentiate between buildings to which cable companies have deployed connections (which are used to provided dedicated services) and buildings to which cable companies have deployed only coaxial cable facilities (which are not used to provide dedicated services).

Moreover, cable companies have a limited ability to compete in the provision of dedicated services even in those locations where they have deployed fiber connections. As Windstream explains, “[t]o the extent that cable companies are beginning to offer dedicated services . . . these cable offerings are available only in the more limited set of buildings where cable providers have their own last-mile fiber access. And even at these locations, cable companies' relatively limited range of managed and individually tailored services has made it more difficult for these companies to expand into the dedicated services markets.”³⁰ As the Joint CLECs explained, the cable companies have themselves candidly admitted that this is the case.³¹

Geographic scope of entry. The incumbent LECs also try to diminish the significance of their monopoly over connections by asserting that competitive carriers deploy facilities in

²⁹ See CenturyLink Comments at 19-25.

³⁰ Windstream Comments at 19-20.

³¹ Joint CLECs Comments at 27-30.

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geographic markets larger than a building.³² While it is true that competitive carriers generally enter a new geographic area by deploying a fiber ring, this in no way means that they can serve every location near the ring. Mr. Merriman’s analysis demonstrates this point. In fact, if competitive carriers could simply deploy connections to most locations in the vicinity of their fiber transport facilities, competitive carriers would have deployed connections to a large percentage of the locations by now. But this is not the case. Moreover, as Drs. Besen and Mitchell found, (i) “even in areas where CLEC providers have facilities, many have failed to acquire any special access purchasers;”³³ (ii) “CLECs with purchasers of special access tend to be few in number in many areas;”³⁴ and (iii) “ILECs still continue to capture a very large share of all special access service volumes in the great majority of census blocks.”³⁵

The incumbent LECs’ pricing practices demonstrate that they do not perceive nearby competitive LEC fiber as a competitive threat. In particular, the results of Dr. Baker’s regression analysis show that, **[BEGIN HIGHLY CONFIDENTIAL]**

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[END HIGHLY CONFIDENTIAL]

³² See, e.g., Verizon Comments at 21.

³³ Declaration of Stanley M. Besen and Bridger M. Mitchell, , Attachment 1, Sprint Comments, WC Docket No. 05-25, RM-10593, ¶ 42 (filed Jan. 27, 2016) (“Besen and Mitchell Decl.”).

³⁴ *Id.*

³⁵ *Id.*

³⁶ See Baker Decl. ¶ 63.

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Transition from DS1s and DS3s to Ethernet. The incumbent LECs attempt to confuse the market analysis by arguing that the growth of Ethernet somehow changes the economics of loop deployment, but this is of course incorrect. The fact that many customers that previously could only be served by TDM technology now may be served by TDM or Ethernet-based dedicated services does not expand the availability of *connections* capable of supporting dedicated services. Because the incumbent LECs derive their market power from their monopoly over connections, a change in the electronics attached to those connections from TDM to Ethernet does not, by itself, affect that market power in any way.

Expert economic analysis. Not surprisingly, numerous economists who have considered these market circumstances have concluded that the presence of competitors with fiber transport facilities near to locations where customers demand dedicated services does not discipline the rates, terms, and conditions on which incumbent LECs offer dedicated services. In his reply declaration, Dr. Baker explains that “the ILECs are not correct in supposing that the presence of a nearby CLEC makes dedicated services market competitive, and prevents ILECs from charging supracompetitive prices for dedicated services.”³⁷ This is so for four basic reasons.

First, it is impractical to connect every potential dedicated services customer in every building in a census block with a fiber ring passing through that census block. This is true for a host of reasons, including, for example, the lack of a node in the census tract, configuration of the fiber for transport rather than to provide service to buildings, insufficient capacity, distance

³⁷ Reply Declaration of Dr. Jonathan B. Baker on Market Power in the Provision of Dedicated (Special Access) Services, ¶ 6 (Feb. 19, 2016) (*attached to* Letter from Dr. Jonathan Baker, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, RM-10593 (filed Feb. 19, 2016)) (“Baker Reply Decl.”).

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from the node to a building, lack of building access or rights-of-way, and insufficient potential revenue to justify the build.³⁸ *Second*, as discussed, a competitive LEC that has deployed fiber transport facilities “near a building has not made the sunk expenditures required to serve that building with its facilities.”³⁹ Incurring the extra costs of loop facilities frequently makes it uneconomic for a competitive LEC to deploy a new connection.⁴⁰ *Third*, where the potential customer has multiple locations that must be served, the competitive LEC must frequently lease facilities from the incumbent LEC to serve many of those locations.⁴¹ As discussed, where this is the case, the competitive LEC faces the risk that the incumbent LEC will charge high wholesale prices for dedicated services at the off-net locations, limiting the competitive LEC’s ability to compete.⁴² *Fourth*, as also discussed, **[BEGIN HIGHLY CONFIDENTIAL]**

[END HIGHLY CONFIDENTIAL].⁴³

Drs. Besen and Mitchell reached a similar conclusion. They explain that “[a] CLEC may have installed fiber in a census block but may not be able to serve any locations therein because,

³⁸ *Id.*

³⁹ *Id.* ¶ 7.

⁴⁰ *Id.*

⁴¹ *See id.* ¶ 8.

⁴² *See id.* ¶¶ 8-9.

⁴³ *See Baker Decl.* ¶ 63.

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for example, it may not operate an interconnection point within the census block. Moreover, a CLEC's network often may be located at such a distance from the customer that the CLEC would be unable to recoup the costs of extending its network facilities from future sales.”⁴⁴ The obvious implication is that the presence of competitive carrier fiber near a location does not constitute the type of potential competition that will discipline incumbent LEC prices.

In an attempt to provide some basis for their claim that nearby competitive carrier fiber facilities represent potential competition that is timely, likely, and sufficient enough to discipline incumbent LEC prices, the ILEC Economic Analysis argues that special access has the characteristics of a “bidding market.” The idea here is that the incumbent LEC may have a large market share **[BEGIN HIGHLY CONFIDENTIAL]** **[END**

HIGHLY CONFIDENTIAL] yet it might still “be effectively constrained by alternative bids submitted by competing suppliers or by the threat of such bids.”⁴⁵ As Dr. Baker explains, however, it is an “exploded myth” that in bidding markets market share does not imply market power and that the existence of two firms in such a “bidding market” implies perfect competition.⁴⁶ In any event, the incumbent LECs’ proposed bidding market theory begs the question of whether, in fact, competitive carriers can offer facilities-based dedicated services to locations near their fiber-transport networks. As explained above, this is emphatically not the case for the majority of locations.

⁴⁴ Besen and Mitchell Decl. ¶ 30; *see also* Baker Decl. ¶¶ 96-106.

⁴⁵ ILEC Economic Analysis at 9.

⁴⁶ Baker Reply Decl. ¶ 12.

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B. “Best Efforts” Services and Fixed Wireless Services Are Not Substitutes for Dedicated Services

As demonstrated by the Joint CLECs and others, neither “best efforts” services nor fixed wireless services are substitutes for dedicated services. The evidence regarding best efforts services is both substantial and conclusive. As Gary Black and Chris McReynolds explained in declarations filed with the Joint CLECs’ comments, Level 3 has found that business customers do not perceive best efforts broadband services to be substitutes for dedicated services.⁴⁷ Other carriers agree. For example, Windstream and XO explain that there are important differences between dedicated services and best efforts services, including the provision of service level assurances, the ability to provide consistent high-speed symmetrical transmission capabilities, the availability of personalized support, and the ability to permit transmission and networking among customers’ facilities.⁴⁸ XO describes the effect of recent changes in best efforts services as follows: “XO has found that while a growing number of smaller businesses with smaller spend are opting for Best Efforts services, its medium-sized business and enterprise customers continue to want Dedicated Services, and Best Efforts offerings have not made significant inroads into Mid-Size and Large/Enterprise Account customers.”⁴⁹ TDS confirms this conclusion, explaining that “[c]able modem service is not an acceptable alternative for businesses needing Ethernet service” because, as a best efforts service, cable modem service cannot provide network availability guarantees close to 100 percent of the time, does not prioritize certain traffic during periods of heavy use, provides service for multiple customers

⁴⁷ See Joint CLECs Comments at 16-17 (describing declarations).

⁴⁸ Windstream Comments at 17-20; XO Comments at 26.

⁴⁹ XO Comments at 26.

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over the same facilities, and because customers wanting 10 Mbps or more “prefer dedicated connections with symmetrical speeds to operate and support cloud-based applications.”⁵⁰ Not surprisingly, Windstream has found that customers are willing to pay higher prices for dedicated services than for best efforts services, even where best efforts services deliver much higher advertised bandwidth.⁵¹

Dr. Baker analyzed the substitutability of best efforts services in light of these and other facts. He found that, “as its price has declined and available bandwidth has increased in many locations, best efforts broadband has often become the preferred option for retail customers with limited demands for service quality.”⁵² But he also found that, “[a]t whatever bandwidth available for best efforts broadband, end users are typically in one camp or the other, preferring either dedicated services or best efforts broadband given the prices and attributes of each.”⁵³ Dr. Baker therefore concluded that, “best-efforts service should be excluded from the relevant market for dedicated services because it ‘lacks the service quality features – particularly availability, reliability, and security – required by most dedicated retail customers.’”⁵⁴

The evidence also strongly supports the conclusion that fixed wireless services do not belong in the same product market as wireline dedicated services. As Messrs. Black and McReynolds explained in their declarations, Level 3 has found that fixed wireless services are

⁵⁰ TDS Comments at 17.

⁵¹ Windstream Comments at 23-24.

⁵² Baker Decl. ¶ 32.

⁵³ *Id.*

⁵⁴ Joint CLECs Comments at 15 (quoting Baker Decl. at ¶ 31).

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not substitutes for wireline dedicated services.⁵⁵ Windstream and TDS have reached the same conclusion.⁵⁶ And, although XO provides fixed wireless services, “XO . . . does not consider wireless media to have the performance capabilities or sufficient reliability for the provision of its Dedicated Services.”⁵⁷ Dr. Baker concluded that “fixed wireless is not generally viewed as a substitute in these settings because of reliability issues arising from congestion, interference and rain fade; the necessity of locating equipment within a clear line of sight; and building access problems.”⁵⁸

III. THE COMMISSION SHOULD REJECT AT&T’S TIRED REPETITION OF CLAIMS THAT THE COMMISSION LACKS THE LEGAL OR ADMINISTRATIVE ABILITY TO TAKE ACTION HERE

AT&T once again tries to scare the Commission into thinking that adopting updated rules to curtail incumbent LEC market power would be too difficult a task, and that, if it does adopt rules, the Commission would be reversed on appeal. AT&T’s repetition of these arguments does not make them stronger. *First*, as explained above, the record in this proceeding clearly demonstrates that there is a market failure that requires a regulatory solution. *Second*, as some of the Joint CLECs have explained, the Commission need not overcome unusual administrative or

⁵⁵ See *id.* at 17-18 (describing declarations).

⁵⁶ Windstream Comments at 30 n.80; TDS Comments at 22 (explaining that TDS tried to provide fixed wireless last mile connections to business locations but encountered a series of operational challenges that provided fixed wireless is “insufficient to meet consumers’ needs for bandwidth and reliability”).

⁵⁷ XO Comments at 25.

⁵⁸ Baker Decl. ¶ 34.

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legal obstacles in order to update price cap regulations for dedicated services.⁵⁹ The Commission also need not make a predicate showing that all of the incumbent LECs' current rates are unjust and unreasonable, as AT&T well knows.⁶⁰ Moreover, there is no basis for AT&T's assertion that applying an updated price cap regime to DSn and Ethernet special access services would be too "daunting" a task for the Commission to undertake.⁶¹

⁵⁹ See Letter from Thomas Jones and Mia Guizzetti Hayes to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, RM-10593 (filed Nov. 9, 2015)).

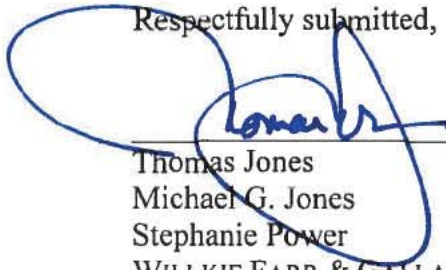
⁶⁰ *Id.* at 3-4 & n.10 (explaining that the Commission would need to make such an affirmative showing only if it were prescribing rates pursuant to Section 205, but the adoption of price caps is *not* a Section 205 rate prescription, as AT&T itself once argued).

⁶¹ *Id.* at 3, 5-6; *see also* Letter from Thomas Jones to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, RM-10593 (filed Aug. 28, 2015)).

IV. CONCLUSION

For the reasons set forth in the comments submitted by the Joint CLECs, and as further set forth above, the Commission should promptly reform the regulatory regime governing incumbent LEC dedicated services in order to prevent incumbent LECs from exercising their market power and to provide American business with greater access to competitive broadband infrastructure and services.

Respectfully submitted,

A large, stylized handwritten signature in blue ink, which appears to be "Thomas Jones", is written over a horizontal line. The signature is somewhat circular and loops around the text below it.

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February 19, 2016

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APPENDIX

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**Before the
Federal Communications Commission
Washington, D.C. 20554**

In the Matter of)	
)	
Special Access for Price Cap Local Exchange Carriers)	WC Docket No. 05-25
)	
AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Internet Special Access Services)	RM-10593
)	

**DECLARATION OF JOHN MERRIMAN
ON BEHALF OF LEVEL 3 COMMUNICATIONS, LLC**

1. My name is John Merriman. I am Vice President of Finance for North America for Level 3 Communications, LLC (“Level 3”). My responsibilities at Level 3 include managing the revenue and capital budget for North America. I have 16 years of experience in various finance roles at tw telecom and Level 3.

2. The purpose of this declaration is to (1) describe the manner in which Level 3 determines whether to build out its network in new geographic areas and to specific customer locations within those areas and (2) demonstrate why, based on these guidelines, it is not economic for Level 3 to build out its network to the majority of commercial buildings where there is demand for dedicated services.¹

¹ For purposes of this declaration, I use the term “dedicated services” as the FCC defined it in the special access data request. *See Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, Order on Reconsideration, 29 FCC Rcd. 10899, App. A at 2 (2014) (defining “dedicated service” as a service that “transports data between two or more designated points, *e.g.*, between an *End User*’s premises and a point-of-presence, between the central office of a local exchange carrier (LEC) and a point-of-presence, or between two *End User* premises, at a rate of at least 1.5 Mbps in both directions (upstream/downstream) with prescribed performance requirements that

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3. When Level 3 deploys local fiber transmission facilities in a new geographic area, it first constructs fiber ring transport facilities and then constructs fiber lateral (*i.e.*, loop) facilities that connect its fiber ring to specific customer locations. Below I describe the manner in which Level 3 determines whether to deploy both new fiber rings and new loop facilities. To illustrate Level 3's decision-making process for loop facilities, I have conducted an analysis of the top ten (by population) Metropolitan Statistical Areas (MSAs)—New York, Los Angeles, Chicago, Dallas-Fort Worth, Houston, Philadelphia, Washington, D.C., Miami, Atlanta, and Boston.

Deploying Fiber Rings

4. When Level 3 has interest in deploying a fiber ring in a geographic area, its marketing team first generates a list of target customers in the area. **[BEGIN HIGHLY CONFIDENTIAL]**

include bandwidth-, latency-, or error-rate guarantees or other parameters that define delivery under a *Tariff* or in a service-level agreement.”).

[END HIGHLY CONFIDENTIAL]

5. Entry involves substantial fixed expenditures, including the costs incurred to build the fiber ring and laterals and install electronics on the circuits. Those fixed costs are the main reason for scale economies in the provision of dedicated services. The cost of deploying a fiber ring varies significantly by geographic location due to differences in both the length of the rings and the cost-per-foot of deployment. A typical Level 3 fiber ring in a central business district is

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6. Level 3's cost-per-foot of deployment varies due to factors such as access to pole attachments, differences in terrain, permitting costs, repaving requirements, and moratoriums due to weather. The cost-per-foot of deploying facilities in a central business district is greater than the cost-per-foot of deploying facilities outside of the central business district.

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Deploying Fiber Loops

7. Once Level 3 has constructed a fiber ring in a geographic area, such as one of the MSAs discussed in this declaration, Level 3 follows certain guidelines for determining whether to deploy fiber loops from that ring to particular customer locations. **[BEGIN HIGHLY CONFIDENTIAL]**

[END HIGHLY CONFIDENTIAL] Potential build-out opportunities to customers that Level 3 does target are examined with respect to the estimated capital expenditure that would be necessary and the expected revenue that would result from the build out. Under its guidelines, Level 3 considers the **[BEGIN HIGHLY CONFIDENTIAL]**

[END HIGHLY CONFIDENTIAL].

8. Level 3 will generally build out its network in response to a particular sales opportunity for customers that meet Level 3's target criteria where the company's overall budget and priorities allow for the capital expenditure, in the discretion of the relevant decision-makers and internal organizations, and where the financial metrics for the build-out are as follows:

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9.

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10. Based on these guidelines, it is rarely possible for Level 3 to deploy its own fiber optic loop facilities to commercial buildings. Table 2 below displays the percentage of commercial buildings to which Level 3 has been able to deploy its own loop facilities in each of the top ten MSAs as of December 31, 2015. The count of total commercial buildings is as of December, 2015 and is derived from data purchased from CoStar Group.

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11. For the purposes of this declaration, Level 3 performed an analysis to identify commercial buildings in each of the top ten MSAs to which Level 3 has not deployed its own loop facilities (“Non-Level 3 Buildings”) but that are potential targets for loop deployment.

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HIGHLY CONFIDENTIAL] It is important to note that the assumption used in this analysis that Level 3 would capture all of the estimated telecommunications spend in a building is highly unrealistic: Level 3 will rarely capture all of the telecom spend in a given building, or even of a given customer in a given building. Accordingly, this analysis produces, and is intended to produce, an overinclusive set of buildings to which Level 3 might plausibly deploy loop facilities. In other words, the number of Non-Level 3 Buildings to which Level 3 might plausibly deploy in the intermediate term in each of these MSAs is *lower than* the number produced by this analysis.

12. Table 3 below displays the results of the analysis set forth above of the commercial buildings to which Level 3 might potentially be able to deploy a fiber loop.

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[END HIGHLY CONFIDENTIAL]

13. These figures demonstrate that Level 3 will not be able to deploy its own loops to the vast majority of commercial buildings in the top ten MSAs. Further, it is important to emphasize that Table 3 overstates the number of buildings to which Level 3 could actually deploy loop facilities. This is so for several reasons.

14. First, as noted above, Level 3 will rarely capture all of the telecom spend in a given building, or even of a given customer in a given building. Indeed, given that enterprise customers frequently purchase dedicated services and other services that Level 3 sells on 3-5 year contracts, the amount of telecommunications spend actually available from potential

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customers in a given building in a given year is likely a fraction of the building's total annual telecommunications spend. Level 3 can only economically deploy a fiber loop where the actual revenues Level 3 secures from a sale of services, plus revenues Level 3 can reasonably expect to win through additional sales to other tenants, satisfies Level 3's target financial metrics.

15. In addition, some customers purchase bundles of services from the incumbent LECs, and will incur penalties if they "break the bundle" by switching to Level 3 for one or more service offerings. Other customers are reluctant to switch when doing so would require them to purchase new equipment. Many customers have made significant investments in legacy equipment at their premises, such as TDM-based private branch exchanges, which they have traditionally used in connection with TDM-based services purchased from the incumbent LECs. Much of this equipment is incompatible with certain IP-based services offered by Level 3. Given the often high price of new equipment, many customers decide to continue purchasing service from the incumbent LEC rather than entering into a service contract with Level 3 that would enable Level 3 to deploy fiber to the customer's location.

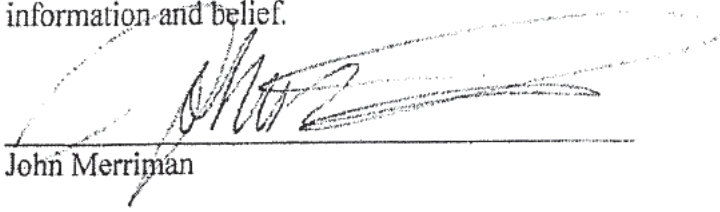
16. Second, even in the small number of locations where it would be economic for Level 3 to deploy loop facilities, Level 3 still must gain access to the relevant building in order to serve its potential customer(s). Level 3 often encounters hurdles when attempting to obtain right of entry into the telecommunications space of a building and sometimes must pay a significant amount for this right. This sometimes prevents Level 3 from serving customers within a given building. In contrast, by virtue of their historical monopolies, the incumbent LECs receive right of entry into the telecommunications space of virtually every building in their service areas. This is simply one of the many advantages that the incumbent LECs have over competitive LECs due to their incumbency.

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17. Finally, when competing for the business of multi-location customers, the cost of leasing off-net facilities from the incumbent LEC to serve some of a potential customer's locations can be so high that Level 3 cannot effectively compete for the customer's business. Loss of such opportunities prevents Level 3 from building fiber to serve those potential customers, even when it might have been economic to deploy fiber to some, or even most, of customer's locations. In this way, high incumbent LEC special access prices prevent Level 3 from building loops to buildings that otherwise meet Level 3's build guidelines.

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I declare under penalty of perjury that the foregoing is true and correct to the best of my
information and belief.



John Merriman

Dated: _____

2/18/16